



Client Bulletin

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July 25, 2008

We're into summer and there has already been plenty of stormy weather on the news! There were even tornadoes reported in New Hampshire and Rhode Island! Well, we also continue to see stormy weather in the capital markets. Of note however, we have just put the offensive team back into play. This comes as 6% of the stocks on the New York Stock Exchange have moved from being controlled by supply to being controlled by demand. With the offensive team back on the field, that means that we have increased our weighting in the stock market.

There are several notable shifts in leadership taking place in the market. As these new trends emerge, you can expect that there will be portfolio adjustments that we will make to take advantage of the best upside opportunities.



Current Thoughts About The Market:

- The energy sector, with strong relative strength since 2002, is beginning to show signs of longer term deterioration. Our newsletters have already discussed the almost vertical rise in price in energy. Now that we've seen recent and distinct signs of problems emerging in this sector, we have elected to get out.
- We have avoided exposure to bank, mortgage, and real estate securities for several years. Both our fundamental and supply-and-demand research clearly indicted that these sectors could be ticking bombs. Overly aggressive accounting practices and unsatisfactory stewardship were very evident, and finally caught up with these sectors.

However, we are now beginning to see opportunities in these out-of-favor sectors. We are also fortunate to be in a position to invest in these sectors in what we believe will be a new era of business conservatism and more responsible stewardship. There remain capitalization problems in the industry, and we will see more write-downs and more failures, but for the first time in years these sectors are beginning to provide more reasonable reward/risk opportunities.
- The international markets have been exceptionally strong relative to the U.S. markets since 2002. This international edge over the U.S. is waning and the U.S. markets may soon be taking the baton.
- The equity markets have put in their worst showing since posting a losing year in 2002, but as in any crisis, opportunity arises. Some of the supply-and-demand indicators we follow are at extremely washed-out levels and reversing up. That suggests for the near to intermediate term, we are much more likely to be near a bottom than a top.
- In July, the Dow Jones Industrial Average, the S&P 500, and other major market indices made yet new lows. However, the main supply-and-demand indicators that we follow (our coaches) did not follow suit. This divergence between the indices and these supply-and-demand indicators is reminiscent of market bottoms in 1982 and 2003.
- The dollar has been in a downtrend since 2002. Foreign currencies have generally been a good investment. More recently, however, the price action between U.S. dollar strength and foreign currency strength has been in a tug-of-war. At some point either the U.S. dollar or foreign currency will win out. We liquidated our position in foreign currencies and will wait and see how this tug-of-war plays out.
- Volatility in the third quarter of 2008, as this is being written, continues right where the first half of the year left off. (continued on next page)

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The first eight out of seventeen trading days saw the Dow Jones Industrial Average record 100 point moves either up or down. Volatility is expected at market bottoms. That is why it is so hard for the general investing public to take advantage of oversold opportunities. This is why we follow our supply-and-demand indicators. They give us a framework and the confidence to invest when things appear to be at their worst. Statistics and hindsight indicate that this is usually the best time to buy.

- Focus is essential. We don't want to become a victim of following the crowd by turning to the financial news media for investment advice. The goal of these media outlets is to get more eyeballs to watch or listen, not manage a portfolio. Our goal is to manage the upside and the downside, reward and risk, in your portfolio. So, we turn off the TV and radio. We instead use fundamental and supply-and-demand research data to analyze what is really happening in the market place to best to position your portfolio.

So, to reiterate, we are on the offensive and back in wealth accumulation mode. Bottoming is a process. This is a time to expect fluctuating values. We hope that we spend several months or more marching down the field and making money.

However, if the demand team fumbles the ball, which could happen, we will not second guess the reality of the market. We will move back to a defensive posture and wait for the next opportunity. Now, however, we will be screening our universe of securities to unearth the best opportunities with good reward-risk ratios. We will adhere to both the buy and sell side of our decision-making process, and let the discipline which has helped us successfully navigate this market continue to be our light in this stormy environment.

At these inflection points there is usually extreme volatility, so you may see some downside before seeing upside in your portfolio values. In moving out of commodities for instance, we moved out after they had begun to erode from their price tops. The fact is that since the Bear market started last Fall, our portfolios are performing much better than all of the major indices. We believe that we are well-positioned going forward. As you know, we do continual due-diligence on every security in your portfolio, and adjust accordingly.

If you have any questions regarding our investment management strategy, or any other related questions for that matter, feel free to contact me and I will be happy to discuss them with you. In the meantime, kick back, relax and enjoy the second half of your summer with family and friends.

Thank you for your business, your interest, and your support.

Bill Baker

William Baker & Associates, Inc.

P.S. If you think this type of analysis would be of benefit to anyone you know, please share this communication with them.